INTERNAL CONTROL SYSTEMS

County Treasurers Conference
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Why do we talk about internal controls then find it difficult to take action?

• Control systems are not uniform.
• They are not tangible.

They are not rocket science but in order to be effective they have to be more than just thoughts in the mind of management.

Summary of the Discussion

- Understanding Internal Control
  - 3 Categories of Objectives
  - 5 Components on Internal Control Systems
  - COSO/Green Book
    - Expanded guidance on the role of those in charge of governance in Internal Control Systems
    - Adjusted for increased dependence on IT
    - 17 principles under the 5 components
- Implementation

Definition of Effective Internal Control

An effective system of internal control requires that:
- Each of the 5 components and 17 principles are present and functioning and,
- The 5 components operate together in an integrated manner.

A major deficiency exists if the county cannot conclude that these are met.

Internal Control Framework

Management's Objectives

- Operations
- Reporting
- Compliance

Internal Control Components

- Control Environment
- Risk Assessment
- Control Activities
- Information & Communication
- Monitoring Activities

Control Environment

- Set of standards, processes, and structures
- Tone at the top
- Integrity and ethical values of the county
- Includes performance measures, incentives, and rewards

Acts as the foundation for a sound system of internal control

Risk Assessment

Risk assessment requires management to consider the impact of possible changes in the external environment and within the county that may render internal control ineffective.

- Many organizations, take a risk-based approach to internal control
- Includes:
  - Risk Identification
 - Risk Analysis
  - Risk Response

Control Activities

Control activities are the actions established through policies and procedures to mitigate risks to the achievement of objectives.

- Preventive or detective in nature
- Manual and automated activities
- Includes segregation of duties

Internal controls
combat fraud and mistakes

Fraud Triangle

- Prevent
  Opportunity

- Detect
  Fraud, Errors
  and
  Omissions

Pressure

Opportunity

Rationalization
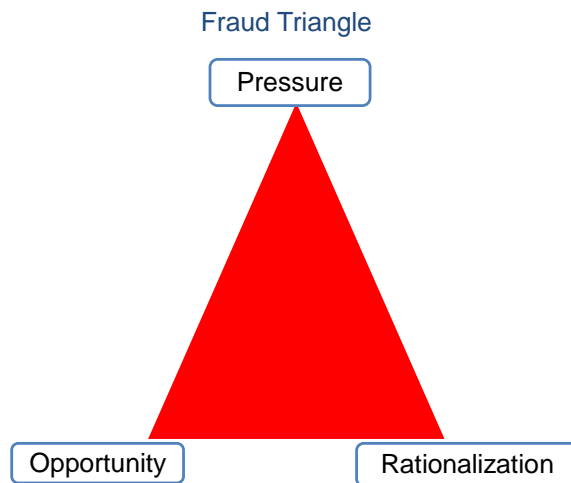
Information and Communication

- Emphasizes importance of quality information
- Volume and sources
- Complexity of processes
- Technology advances
- Greater interaction with 3rd party vendors
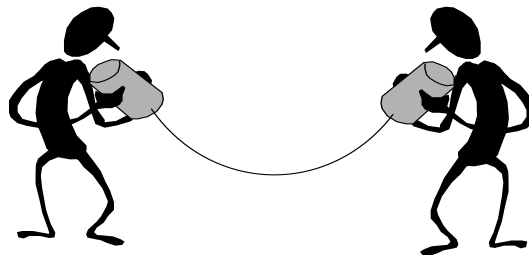
Monitoring Activities

Ongoing Evaluations	Separate Evaluations
• Built into the business process at various levels • Timely information	• Conducted periodically • Frequency will depend on assessment of risks and effectiveness of ongoing evaluations

New Principles

COSO/Green Book clarifies requirements for effective internal control with the 17 new principles

• Principles relate to a component of the internal control system
• Not required
• Common sense

Control Environment

1. The county demonstrates a commitment to integrity and ethical values.
2. Governing boards demonstrate independence from management and exercises oversight of internal control system.
3. Management establishes, with board oversight, an organizational structure, assign responsibilities, reporting lines, and delegate authority to achieve the county's objectives.
4. The county demonstrates a commitment to attract, develop and retain competent individuals.
5. The county holds individuals accountable for their internal control responsibilities.

Risk Assessment

6. The county specifies objectives with sufficient clarity to enable the identification and assessment of risks relating to objectives.
7. The county identifies risks to the achievement of its objective across the entity and analyzes risks as a basis for determining how the risks should be managed.
8. The county considers the potential for fraud in assessing risks to the achievement of objectives.
9. The county identifies and assesses changes that could significantly impact the system of internal control.

Control Activities

10. The county selects and develops control activities to achieve objectives and respond to risks.
11. The county selects and develops general control activities over technology to support the achievement of objectives.
12. The county deploys control activities through policies that establish what is expected and procedures that put policies into place.

Information and Communication

13. The county obtains or generates and uses relevant, quality information to support the functioning of internal control.
14. The county internally communicates information, including objectives and responsibilities for internal control, necessary to support the functioning of the internal control.
15. The county communicates with external parties regarding matters affecting the functioning of internal control.

Monitoring Activities

16. The county establishes and operates monitoring activities to monitor the internal control system and evaluate the results.

17. The county evaluates and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the governing boards, as appropriate.

Take it Step by Step and see where it leads you!

1. Control Environment
2. Risk Assessment
3. Control Activities
4. Information and Communication
5. Monitoring

Documentation

Start with documenting the 5 components in significant areas first.

- Cash handling

- Management's Goals
  - Customer Service
  - Compliance with Laws and Regulations

Find where there is risk that is not mitigated by internal control

- This is Risk identification
- Perform your risk analysis
- Respond to the risk
  - Implementing controls
  - Insurance
  - Acceptance of the Risk

Are you going to "trust" or **"make sure"** things are done right in your office?